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RUEHBU/AMEMBASSY BUENOS AIRES 3083
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RUEHMN/AMEMBASSY MONTEVIDEO 2636
RUEHSG/AMEMBASSY SANTIAGO 2332
RUEHLP/AMEMBASSY LA PAZ 3741
RUCPDOC/USDOC WASHDC 3046
RUEATRS/DEPT OF TREASURY WASHDC
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UNCLAS SECTION 01 OF 02 SAO PAULO 000115

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DEPT OF TREASURY FOR JHOEK

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TAGS: ECON EFIN EINV BR
SUBJECT: BRAZILIAN STOCK EXCHANGES BOVESPA, BM&F IN MERGER TALKS

REF: 07 SAO PAULO 0899

¶1. SUMMARY: Bovespa Holding, the company that controls and manages the Sao Paulo Stock Exchange, and Brazil's Commodities and Futures Exchange (BM&F) informed Brazil's Securities Commission (CVM) and investors on February 19 that the two companies had initiated negotiations for a possible merger, but stressed that a deal had not yet been reached. Their press statement said the two sides would announce the results within 60 days. A merger would make the resulting company the second largest exchange in the Western Hemisphere behind the Chicago Mercantile Exchange (CME). In addition to optimizing costs and increasing profits and reliability for investors, the merger could potentially boost investor confidence and attract more foreign investment. The proposed merger is another example of companies taking advantage of the current strength of the Brazilian economy to make long-term decisions that should reap long-term benefits. END SUMMARY.

¶2. On February 19, Bovespa Holding and Brazil's Commodities and Futures Exchange (BM&F) issued a statement to investors and the Securities Exchange Commission (CVM) that the two had initiated formal talks for a merger. Neither Bovespa Holding Chief Executive Gilberto Mifano nor BM&F Chief Executive Edemir Pinto has guaranteed that any agreement will be reached from these discussions. Both noted that the two companies will not give any further information before the end of the sixty-day period, during which both parties are restricted from initiating transactions with third parties. Press reports indicate that the two companies want to follow what the Chicago Mercantile Exchange (CME) did in 2007 when it merged with the Chicago Board of Trade, a step towards consolidating the world's stocks and futures exchanges.

¶3. The latest announcement follows last year's phenomenal stock performance and the initial public offerings (IPO) of both companies. Bovespa Holding raised USD 3.8 billion in October with its IPO, which was Brazil's largest ever (Ref). BM&F then accumulated USD 3.4 billion in its IPO only a month later. Following their IPOs, the stock prices of both institutions climbed 52 and 22 percent respectively in 2007; however, in the first two months of 2008 both stocks had dropped back down to their IPO price ranges. The market has reacted positively to the merger news with both companies' stocks climbing approximately ten percent each.

¶4. Trading volume has expanded strongly in recent years on both exchanges as international investors have moved into emerging market assets. The consulting firm Economatica estimated the combined value of the merger at USD 18.5 billion, surpassing the New York Stock Exchange (NYSE). Their current estimate is that Bovespa alone is worth USD 10 billion, well above many emerging market exchanges. For example, the Indian exchange is currently valued at USD 1.2 billion and the Chinese exchange at USD three billion. (Note: In October of 2007, prior to BM&F's IPO, the CME took a 10 percent stake in BM&F for two percent of CME. BM&F is the fourth largest futures exchange in the world in terms of contracts negotiated. End Note.)

¶5. The press and local financial interlocutors underscored the benefits of a merger which include reduced operating and administrative costs, as well as facilitation of shares and futures trading. They also point to a reduced workforce and the potential to leverage business synergies. Mauricio Oreng from Itau Bank told Econoff that the merger would be a net positive for Brazil's economy, and would elevate Brazil's role in world financial markets as well as potentially leading to regional consolidation of stock exchanges. Oreng opined that the merger would attract more foreign investment because Brazilian markets are well regulated and investors are enthusiastic about merger negotiations. Professor Alcides Leite from the Trevisan Business School said that the merger would provide the market with another very liquid and credible asset. The Vice President for Treasury Operations Julio Sequera told Econoff that the merger would leverage economies of scale and existing synergies, however, that the merger depended on market conditions to succeed. He expects the merger talks to result in a unification of the two exchanges.

¶6. COMMENT: The proposed merger of Brazil's largest exchanges looks

set for a warm reception from shareholders who expect to benefit from cost savings and lower trading fees. This is yet another example of how Brazil's strong economic performance is changing private sector investment and business strategies from reacting to short-term situations to making long-term decisions. END COMMENT.

¶7. This cable has been cleared by the Embassy in Brasilia.

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